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Forfeiture of Oil and Gas Lease for Breach of Covenant

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quoted, but Judge Miller beyond a doubt gave to it the interpretation hereinbefore stated as the correct one. He says:

"This construction may not necessarily work a repeal of section 38. It may perhaps still be applied with its full force to the other provisions of section 34; but this question is not presented and we do not decide it."

Perhaps the *dictum* in *Leiter v. American-La France Fire Engine Co.* either is inadvertent or else was based, without full consideration, upon the ambiguous syllabus of *Speidel Grocery Co. v. War-*
der. —L. C.

FORFEITURE OF OIL AND GAS LEASE FOR BREACH OF COVENANT.—The Supreme Court of Kansas recently has affirmed a judgment canceling an oil and gas lease for breach of an express covenant to complete a well on the premises within sixty days.¹ The lease in question was for a term of one year and as long thereafter as oil or gas should be produced or operations continued. The lessees covenanted "to complete a well on said premises within sixty (60) days from the date hereof, or in case of a failure to complete a well within the time above specified, to pay to the first parties fifteen dollars (\$15) in advance for each additional month such completion is *unavoidably* delayed from the time above mentioned for the completion of such well, until the well is completed or this contract is surrendered, as is hereinafter provided; . . ." The lessees did not begin a well within sixty days from the date of the lease. Two days after the expiration of the sixty day period the lessor served notice on the lessees that the lease was forfeited for failure of the lessees to perform the covenants and conditions therein. Suit was then started to cancel the lease. The trial court found that the lessees had made no effort to develop the premises within sixty days, and that this failure to do so was not the result of unavoidable delays. The court held that the proper construction of the covenant was that the lessees were bound to complete a well within sixty days, except that its completion might be deferred in case there was unavoidable delay, and that by reason of the omission and neglect of the defendants to keep and perform this covenant they had forfeited their rights. Judgment was entered canceling and setting aside the lease. The Supreme Court affirmed this judgment on the sole ground that the defend-

¹ *Waters v. Hatfield*, 190 Pac. 599 (Kan. 1920).

ants had made a breach of their covenant to complete a well within sixty days, the court stating its conclusion as follows: "It was an express covenant that formed a part of the consideration for the granting of the lease, its violation warranted the judgment canceling the lease, and it follows that the judgment must be affirmed." Is there any ground upon which the judgment can be sustained?

An ordinary lease cannot be forfeited for a mere breach of covenant.² The same rule has been quite consistently applied to oil and gas leases though they are not true leases but create profits *a prendre*.³ In the case of ordinary leases in the absence of statutory provisions a forfeiture usually can be declared only for breach of an express condition. In the case of oil and gas leases a forfeiture may also be declared for breach of an implied condition. Two of the situations under which a court will sometimes imply a condition in an oil and gas lease may be apropos to this note. First, where there is no express provision in an oil and gas lease as to how or when the lessee is to drill for oil and gas on the premises, it is said that there is an implied covenant that he is to prospect for oil and gas with reasonable diligence and also an implied condition that if he fails to perform this duty, the lessor may forfeit the lease.⁴ The courts say that considering the instrument as a whole, it appears that the primary purpose of the lessor in entering into the lease was to have the premises prospected for oil and gas and if these minerals were found, to have them produced so that he would realize the royalties therefrom. Hence it is inequitable to permit the lessee to hold the lease without prospecting for oil and gas and so to defeat this primary purpose. Consequently, the condition is implied as above stated.⁵ Second, if at any time during the continuance of the lease, wells are drilled on neighboring lands near the boundaries of the premises so as to drain or threaten to drain oil and gas therefrom, it is held it is the implied duty of the lessee to drill offset wells to prevent such drainage, and if he fails in the performance of this duty, the lessor may declare a forfeiture.⁶ It is said the intent of the parties was to produce the oil and gas from the premises

² See *TIFFANY, LANDLORD AND TENANT*, 1364.

³ *Howerton v. Kansas Natural Gas Co.*, 81 Kan. 553, 108 Pac. 813 (1910). See 25 W. VA. L. QUAR. 311-325.

⁴ *Gadbury v. Indiana Consolidated Gas Co.*, 162 Ind. 9, 67 N. E. 259 (1903); *Brewster v. Lanyon Zinc Co.*, 140 Fed. 801 (1905); *Lovett v. Eastern Oil Co.*, 68 W. Va. 667, 70 S. E. 708 (1911).

⁵ Note 45, *supra*.

⁶ *Kleppner v. Lemon*, 176 Pa. St. 502, 35 Atl. 109 (1896).

and not to allow it to be lost by drainage through adjoining lands, consequently the lessee cannot hold the lease without protecting the boundaries to the irrevocable damage of the lessor.⁷ Whether on principle it is proper to imply the above conditions in oil and gas leases is not under consideration. The fact is, such conditions are sometimes implied.

Can the judgment in the principal case be justified either on the ground there was an implied condition, that if the lessees failed to develop the premises for oil and gas by drilling a well within sixty days, the lease might be forfeited for breach of this condition, or on the ground that there was an implied condition in the lease that the lessor might forfeit if the lessees failed to protect the premises from drainage? The objection that the judgment in the case would be a decree in aid of a forfeiture may be disregarded. While it has been said that a court of equity will never enter a decree in aid of a forfeiture,⁸ the fact is that in controversies arising out of oil and gas leases a court of equity will and sometimes does enter a decree in aid of a forfeiture.⁹

In the principal case the duty of the lessees to prospect for oil and gas is set out in the express covenant, consequently, if there is an implied condition as to development, it must be a condition that if the lessees fail to perform their covenant to complete a well within sixty days, unavoidable delays excepted, the lessor may forfeit the lease. It would certainly not be reasonable to imply a condition requiring the lessee to prospect for oil and gas with reasonable diligence where there is such a covenant. Had the word "unavoidably" been omitted from the covenant, then there could be no implied condition whatever because the lessees would have had the option, by the express terms of the instrument, of completing a well or paying fifteen dollars per month for each month such completion was delayed.¹⁰ But as the covenant in question was construed by the court there is no express provision in the lease squarely inconsistent with the implication of the condition

⁷ Perhaps it is accurate to say there are two distinct implied conditions. It is probably in fact only one condition, i. e., that the lessor may forfeit if the lessee fails to perform his duty to prospect for and produce oil and gas with reasonable diligence. The fact that there is drainage perhaps is only an element bearing on the question as to what is reasonable diligence. See cases cited in notes 4 and 6 *supra*, and also note in 34 L. R. A. N. S. 34.

⁸ See POMEROY, EQUITY JURISPRUDENCE, 4 ed., §§ 459, 460.

⁹ Many cases which discuss the subject are collected in the notes in 28 L. R. A. N. S. 959; 34 L. R. A. N. S. 34; 38 L. R. A. N. S. 134.

¹⁰ Kachelmacher v. Laird, 92 Oh. St. 24, 110 N. E. 933 (1915); Greek v. Wylie, 109 Atl. 529 (Pa. 1920); Carper v. United Fuel Gas Co., 78 W. Va. 432, 89 S. E. 12 (1916); Howerton v. Kansas Natural Gas Co., *supra*.

suggested above. It is submitted that whatever justification there may be for implying such a condition in the case of a lease for a term of several years, there is none in the principal case where the term was for one year only and the lessees were required by the terms thereof to complete a well before the end of that year. The land would be free from the lease in the course of one year unless at least one well was completed and could then be leased to some one else. The lessor had received the sum of \$520 for the lease (more than the usual annual royalty on a gas well) and since a well was not completed within sixty days, he could have recovered damages in an action at law for breach of the covenant.¹¹ If the royalty provided in the lease was, as is customary, an annual sum of a few hundred dollars—a point as to which the opinion of the court is silent—then the damages for the breach of this covenant could not exceed the annual sum to be paid for one gas well for one year, at most a few hundred dollars. Where the damages to the lessor are necessarily so insignificant, it is submitted that a court ought not to resort to such a drastic action as to imply such a condition and then enter a decree in aid thereof.

If we decide that the covenant to complete a well within sixty days cannot be made a condition by implication, the question then arises as to whether there can be an implied condition as to drainage. While the implication of such a condition may seem rather unusual yet, where the land is under lease for a term of years by the terms of which the lessee is not bound to develop during said term, the oil or gas may be partially or wholly drained from beneath the premises through wells on neighboring land, and thus entirely lost to the lessor. Since the lessor usually gets only a small rental during the time the development is delayed, he thus suffers irreparable injury. Consequently, there is a strong practical reason for giving relief to the lessor in such case, and this has been accomplished through the implication of a condition. In the principal case it appeared that the premises were in an extensive gas field and there was a very large gas well within three hundred feet of the premises and another within a quarter of a mile. Hence there probably was some drainage of gas occurring. In order to have complied with such an implied condition the lessees would probably have been compelled to drill one well to offset the near-

¹¹ *Howerton v. Kansas Natural Gas Co.*, *supra*. This case held that the lessor, before he could have a decree canceling the lease, must show affirmatively that he has no adequate remedy at law. The principal case seems to disregard this prior decision.

est gas well. As they did not do so, if drainage were proved, the lessor's damages could not exceed the amount of the royalty on one gas well for one year, or a few hundred dollars. Here again, it appears that the damages to the lessor were very small and that he might have recovered damages in an action at law. By allowing a forfeiture the lessees lost what must have been a very valuable leasehold for which they had paid a cash consideration of five hundred and twenty dollars.

Under such circumstances the court ought not to announce a new rule of law which has the effect of destroying a valuable lease to the great damage of the lessees and the very great enrichment of the lessor.¹²

It is to be regretted that such uncertainties as we find here are still injected into the law governing oil and gas leases which is already badly confused. In deciding such a controversy between two parties it is even more important to follow established legal principles than to do justice between the parties to the particular suit because all other persons in the state having interests of like nature must govern themselves by the law derived from such principles. Such sudden departures, which cannot be anticipated even by skilled lawyers, are disastrous. It is submitted that the judgment in the principal case is not in accordance with law¹³ and has not even the merit of being equitable as between the parties.

—J. W. S.

¹² It might be suggested that the so-called lease amounted to a mere personal contract and the lessees had made a substantial breach and therefore the lessor had a right to rescind. The logical result of this would be that the oil and gas lease passed to the lessees no right in the land. This, it is submitted, is not a defensible position though *dicta* can be found in the Kansas decision which tend to support it. However, the law of the state seems to be that such a lease creates an incorporeal hereditament. See 18 MICH. L. REV. 765, and cases there cited.

¹³ No provision in the Kansas statutes has been found which authorizes forfeiture for breach of such a covenant.